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Financial Digest

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Analysis of Business Trends Plus Selected Financial Indicators

The Federal Reserve . . .

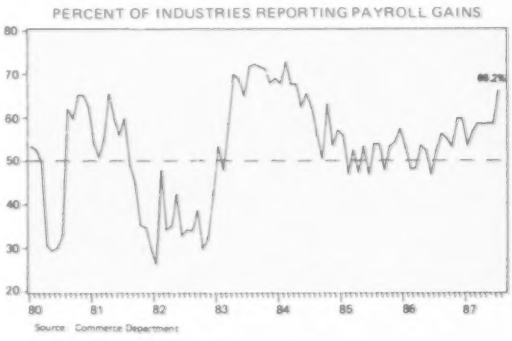
As summer draws to a close in the northern hemisphere, the seasons may not be the only thing about to shift gears. So, too, may monetary policy, if recent trends in the economy, the labor and commodity markets and the dollar persist. This is because with the pace of business picking up, the labor market tightening as nearly full employment approaches (Financial Digest–August 17, 1987), industrial commodity prices rising and the dollar softening in the foreign exchange markets, several key harbingers of an adverse swing in inflation expectations, if not the inflation rate itself, are again appearing on the economic horizon. If they persist, and upcoming business statistics confirm the economic acceleration, prospects for a modest policy tightening in coming weeks will grow.

To be sure, the usual degree of uncertainty surrounds the question of just how well the economy is doing. But the release of several upbeat business statistics in recent months has shifted the burden of proof away from those who believe that the economy has been expanding at a generally acceptable clip, to those who think it is only "muddling through." For despite the fact that progress in reducing the nation's trade deficit continues at a snail's pace, and the trade imbalance remains a heavy drag on economic activity, the overall tone of business in general, and in the goods-producing sector in particular, seems to be improving.

For example, strong gains in personal consumption expenditures, industrial production and capacity utilization rates, all in July, are just some of the latest indications of the economy's added zest. Since they come on the heels of hefty upward revisions to the initially-reported numbers for such June statistics as retail sales and industrial production, it looks like the economy is, and has been, performing much better than originally thought. What is more, since non-defense capital goods orders and manufacturers backlogs are expanding at a rapid clip, industrial production, already rebounding from its 1985-86 lethargy, should remain robust for some time.

. . . May Soon Decide . . .

Perhaps the most telling indication of today's improved business climate is the sharp jump in the number of people working, especially in the manufacturing industries. Turning again to July, more than 300,000 net new jobs were generated economy-wide–nearly four times the preceding six-month average–while the unemployment rate fell to a nearly eight-year low of six percent. Manufacturing employment soared



by some 70,000, reversing just about 60 percent of the 117,000 manufacturing jobs lost in all of 1986. Not surprisingly, with industrial production rebounding and factories again hiring, some two-thirds of all manufacturing industries surveyed by the Commerce Department are now reporting payroll gains, the highest percentage in over three years (see chart).

If there is a drawback to all this, it's on the price front. This is because at some point too much economic vigor could produce such unwanted side effects as capacity constraints, sharply escalating wages and, eventually, higher rates of inflation. Although some might think the chances of this occurring anytime soon are slim, citing as evidence the subdued rise of both consumer and producer prices in July, the fact remains that consumer prices have increased at a five percent annual clip so far this year, while producer prices, even excluding volatile food and energy costs, are increasing at their fastest rate since 1981.

What is more, industrial commodity prices, often viewed as a harbinger of future price trends, continue to advance briskly. Over the

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past three months, for example, they have increased at a nearly 15 percent annual rate. Over the past year, they are up by better than 35 percent, and are now back to just about where they stood at their early 1984 highs. If such price trends are left unchecked, wages may soon begin to play catch-up, setting the stage for a wage-price spiral which everyone—especially central bank policymakers—wants to avoid.

. . . To Tighten Monetary Policy

If this isn't disturbing enough, two other recent developments are adding to inflation concerns. One is the renewed slump of the dollar in the foreign exchange markets; the other is the likelihood of a larger Federal budget deficit in fiscal 1988. Of more immediate importance, a back-to-back monthly widening of the trade deficit in May and June is prompting another bout of periodic dollar weakness—threatening to propel import prices even higher and to dampen the appetite of foreign investors for U.S. dollar denominated assets.

This, in turn, could spell trouble for the credit markets in the months ahead, espe-

Short Term Paper Outstanding

(Millions of Dollars)

Time Deposits of $100,000 or more Weekly Reporting Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (8/12/87)	164,238	– 440	+ 9,945
New York City (8/19/87)	37,081	+ 225	+ 3,707
Commercial Paper (8/19/87)	346,079	+ 127	+ 23,895

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (8/12/87)	269,748	+ 109	+13,436
New York City (8/19/87)	56,527	– 26	+ 588

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (8/12/87)	788,826	– 208	+50,890
New York City (8/19/87)	172,102	– 174	+17,082

Financial Markets

	Friday 8/28/87	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.48%	+ .21	+ 1.31
180-Day Bills†	6.62	+ .10	+ 1.43
Longest Bills†	7.17	+ .21	+ 1.93
Recent Issues:			
7 3/4S 8/15/87	7.96	+ .25	
7 7/8S 6/30/91	8.24	+ .06	
8 5/3S 8/15/97	9.01	+ .26	
8 7/8S 8/15/17	9.18	+ .21	
Municipals:			
Bond Buyer–20 Bond Index* (8/27/87)	7.80%	– .01	+ .87
Blue List Total ($ Million)	$1,772	+ $ 210	+$ 140
30-Day Visible Supply ($ Million)	$ 984	– $2,137	–$ 24
Total	$2,756	– $1,927	+$ 116
Corporates:			
Moody's Aa Composite (8/27/87)	9.89%	–0–	+ .72
30-Day Visible Supply ($ Million)	$4,487	+ $ 94	+$3,256
Stocks:			
Dow-Jones Averages:			
Industrials	2,639.35	– 70.15	+741.01
Transportation	1,062.04	– 24.63	+289.91
Utilities	205.01	– 5.58	– 14.14
65 Stocks	963.88	– 24.76	+227.51
N.Y.S.E. Composite Index	182.99	– 4.51	+ 37.67
N.Y.S.E. Avg. Daily Vol. for Week (000's)	175,814	– 8,896	+44,712

*34% Taxable equivalent 11.82%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 8/28/87	Week Ago
Overnight	6.88%	6.38%
1 month	7.00	6.69
3 month	7.06	6.94
6 month	7.31	7.19
1 year	7.81	7.63
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 yrs.)	8.65%	8.65%
Long Term (10 yrs.)	9.42	9.42

FOREIGN EXCHANGE SPOT RATES

New York Opening (8/28/87)	Currency Per U.S. $	Week Ago
Canada	1.3211	1.3268
France	6.0660	6.0940
Germany	1.8165	1.8235
Italy	1315.75	1320.75
Japan	142.65	143.07
Mexico	1500.00	1481.00
Switzerland	1.4965	1.5095
U.K.*	1.6260	1.6252

*U.S. $ per U.K. pound

MH TRADE-WEIGHTED DOLLAR (8/28/87) (Adjusted for Inflation)	Change Since Week Ago	Change Since 2/27/85
	+0.1%	–3.0%

cially since they will almost certainly be called upon to finance a much larger Federal deficit in the fiscal year beginning October 1. Although the red ink may be trimmed by as much as $60 billion in the current fiscal year, largely due to such transitory factors as a one-time surge in capital gains receipts due to tax reform and asset sales, the fiscal 1988 outlook isn't nearly as good. With the Administration and Congress unable to hammer out a credible deficit reduction program, the budget shortfall may rise from some $160 billion this fiscal year to at least $175 billion next year.

Against this backdrop, near-term economic and price trends may be more thoroughly analyzed than usual. If they reinforce the view that the economy is strengthening and the labor market tightening, the Federal Open Market Committee may opt to tighten policy somewhat at its late September meeting. This could diminish the likelihood of the economy "overheating," curb inflation expectations and bolster the dollar, not to mention send a message to any doubters of Fed Chairman Greenspan's inflation-fighting commitment. ■

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 8/26/87	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	214.137	+ .651	+20.495
Loans to Depository Inst.	.912	+ .387	+ .025
Float	.525	− .356	− .208
Total Reserve Bank Credit	230.982	+ .015	+20.292
Treasury Deposits with Federal Reserve Banks	3.116	− .058	− .168
Currency in Circulation	216.570	− .787	+15.970
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	182.077	+ 2.602	+26.786
	8/26/87		
Member Bank Reserves:			
Total Reserves Held	57.281	− .058	+ 6.785
Excess (Deficiency)	1.145	+ .352	+ .278
Net Free Reserves	.554	+ .205	+ .082

Monetary Aggregates †		% Change Since 3 Months Ago*	% Change Since Year Ago
M1 (8/17/87)	750.7	− 1.6‡	+ 9.9‡
M2 (July '87)	2,846.0	+ 1.1	+ 5.7
M3 (July '87)	3,572.5	+ 3.8	+ 6.1
Domestic Nonfinancial Debt (1st Q'87)	7,805.2	+ 6.4	+ 11.7

†Seasonally adjusted.

*Seasonally adjusted annual rate.
‡Four-week moving average.

New York Money Market

Offering Rates 8/28/87	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	6.30%	6.36%	6.76%
* Federal Agencies	6.70	6.80	6.93
* Municipal Notes—High Grade (34% Taxable Equivalent)	6.21	6.52	6.82
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	6.93	7.20	7.90

‡Finance Company Paper—Prime

5- 14 days	6.65%
15- 29 days	6.63
30- 59 days	6.70
60- 89 days	6.70
90-179 days	6.74
180-239 days	6.65
240-270 days	6.65

‡* Bankers' Acceptances

Sep.	6.80%
Oct.	6.80
Nov.	6.90
Dec.	6.90
Jan.	6.90
Feb.	6.90

‡Industrial Paper—Prime

30- 89 days	6.69%
90-120 days	6.85

†Federal Funds Effective Rate 6.85%

‡Discount basis. *Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	2nd Q'87	$ 4,448r	$ 4,378	$ 4,212
Gross National Product (1982 Dollars)*	2nd Q'87	$ 3,794r	$ 3,772	$ 3,705
Percent Change, Annual Rate	2nd Q'87	2.4r	4.4	0.6
Change in Consumer Prices*	Jul '87n	2.4% (1)	4.8% (1)	0.0%
Change in Producer Prices*	Jul '87	2.4%	2.4%	− 9.6%
Civilian Employment (Thousands of Persons)†	Jul '87	112,727	112,257	109,887
Unemployment as % of Civilian Labor Force†	Jul '87	6.0%	6.1%	7.0%
Personal Income*	Jul '87n	$ 3,738	$ 3,723r	$ 3,540
Leading Indicators Composite Index (1967=100)†	Jun '87	190.4	188.9	178.3
Industrial Production Index (1977=100) †	Jul '87	129.8	128.8	124.9
Net Change in Consumer Installment Credit †	Jun '87	$ 3.46	−$ 0.32	$ 5.01
U.S. Merchandise Trade Balance	Jun '87	−$ 15.71	−$ 14.04	−$ 13.25
Plant and Equipment Expenditures*	3rd Q'87	$397.06(a)	$392.02(c)	$374.55
Private Housing Starts (Thousands of Units)*	Jul '87n	1,611	1,597r	1,786
New Construction Expenditures*	Jun '87	$ 390.1	$ 394.3	$ 371.6
Total Business Inventories †	Jun '87	$ 674.2	$ 671.6	$ 654.1
Total Business Sales †	Jun '87	$ 453.1	$ 446.3	$ 422.0

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.
(1) Indicates new series.

The Letter of Credit Comes of Age.

For generations, there was not much change in the way importers handled their L/C's. From sending an application to checking on a transaction's status, the process of paperwork and phone calls could take days to complete.

Now Manufacturers Hanover Trust is bringing the L/C into the electronic age with the Electronic Letter of Credit Service. Allowing you to prepare and transmit letter of credit transactions directly to us via Personal Computer. And obtain up-to-the-instant computer reports on your letter of credit activity. Swiftly. Accurately. Securely.

With our Electronic Letter of Credit Service your instructions are acknowledged in seconds, and processed without delay. Opening the way to an early delivery of your shipment—and a savings in time and money.

You can track the status of your L/C's and acceptances through our on-line inquiry capability. A unique feature of which allows you to generate reports in standard formats or to design your own.

Add to all of this the assurance that our dedicated team of trade professionals stands ready to give you prompt answers to all your questions.

So put some byte into your L/C with our Electronic Letter of Credit Service. It's one of a number of products that is opening up a new age in banking.

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